Interview: Enerplus' Jo-Anne Caza on Dividend Policy and Oil Prices

Description

In part two of my interview with **Enerplus** (TSX:ERF, NYSE:ERF) VP of Investor Relations Jo-Anne Caza, we discuss the company's decision to cut its dividend last year and what its future payout might look like.

Below is the transcript of our conversation; it has been lightly edited for clarity. You can find part one of our conversation here.

Baillieul: As a former royalty trust, dividends are particularly important to your shareholder base. Obviously the 50% distribution cut we saw in 2012 was pretty painful.

Can you walk us through your thought process as to how you relayed that message to shareholders. And do you think Enerplus' management team learned anything from that experience?

Jo-Anne Caza: The cut as you said back in 2012 was very painful. But it's not something that we do lightly. We realize that investors are looking for stability in the dividend. They want some certainty around that.

To be clear we've always indicated that we are a commodity based business. And if we see significant fluctuations in the underlying commodity that's going to have an impact on our cash flow and our ability to pay a dividend.

As we went through 2012 we saw this collapse in natural gas pricing at a very quick rate. And we also saw some weakening of crude oil prices at the same time and we said you know it comes back down to affordability and we can't afford the dividend at the current level that it's at.

In our history we have revised our dividend previously. It has come down from its high of around $0.40 per share or so and it's really occurred as we seen this real collapse in gas prices over the last five years or so.

As we change the business model as well to deliver organic growth it requires more capital. So more of the cash flow needs to go to the asset base today than it would've been done under the royalty trust model because our growth was coming through acquisitions.

We've tried to be very transparent to our shareholders to say we are a commodity based business and in this kind of commodity price environment we either comfortable we our dividend where it's at. But if you see significant fluctuations in commodity prices, that will have an impact on our cash flow. This will also ultimately have an impact on our capital spending and our dividend as well.

In 2012 we cut our dividend in half. CAPEX [capital expenditures] was kind of locked and loaded already for the year at that point in time. But then as we move into 2013 we had a fairly significant cut in our capital program as well.

Ultimately what we want to do to preserve the financial strength of the company and ensure that we are not running up our balance sheet. Using debt to fund a dividend which is in nobody's best interest.

I think as painful as it was the market was expected it because at the time of the cut the stock was yielding 15% or 16%. So that market was saying you can't afford this payout in this of commodity price scenario.

Since then we thought we've seen good performance in terms of delivering on our promises of delivering organic growth and keeping the balance sheet very strong. And continuing to focus the asset base by selling non-core assets and redeploying those proceeds to some of the other plays within the portfolio and still meeting on our production targets.

And I think the market has responded well – we've seen a very good appreciation in the share price through 2013. So I think we have regained some investor confidence in the marketplace. [In the market's view] Yes, we can actually we can actually excel and this business strategy of growth and a dividend. And we're much more confident of the stability of the dividend today versus where it was previously.

Our dividend would represent somewhere around 20% to 25% of our cash flow our funds flow which we think is a very manageable level. And we think that's competitive with some of the larger companies that maybe have share buybacks. So we think it is a reasonable level and it's giving us cash flow with the reminder to fund our growth prospects.

We'll still outspend our cash flow a little bit but we have pre-funded much of that with some of the asset sales we did during the back-end of the year and another one that just closed here last week. The balance sheet remains here strong position and we think the sustainability overall of our business has improved dramatically where it would have been at that time in 2012 when we had to make those changes.

Baillieul: I wanted to ask if you think you gotten buy-in from some of your larger shareholder regarding your company's new strategy. But I think given the fact that the stock just hit a new 52- week high today, the answer is sort of self-evident.

Just continuing on the dividend theme, we're going to see a lot of production growth in upcoming quarters. What's management's philosophy in terms of capital allocation? Will much of that cash flow growth be reinvested back into the business or can we expect that to be returned to shareholders?

Caza: Ultimately, long term thinking would be as we continue to grow production that cash flow grows and we should be in a position to increase the dividend. We're not there today. And I think in order for us to get there we need to see stronger natural gas prices and greater production volumes.

Our focus this year is deliver production growth to the tune of 10%. That may be a little bit more than what we might need. But we think that's affordable and we think we got a good financial plan that will allow us to get there.

When we think about capital allocation it's really about investing those areas that will give us the greatest economic returns.

10% production growth this year delvers somewhere around 5% cash flow growth. Our outlook this year is crude oil prices are a little lower than they were last year and differentials are a little wider than they were last year. That's why the cash flow growth is a little more muted than production growth. I think the analyst consensus is for a $800 million or so increase in cash flow or funds flow year-over-year in 2014.

From a capital spending perspective our Bakken assets in North Dakota will still attract the lion's share of our capital spending somewhere around 40% or so. And again we're looking at rates of return on those projects in the 50%, 60%, 70% range.

Coming up next…
The North Dakota Bakken has been one of the biggest oil discoveries in American history. In part three of my conversation with Jo-Anne, we dig a little deeper into the company's operations there.

CATEGORY

1. Investing

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Date
2025/08/26
Date Created
2014/01/22
Author
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